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C O N F I D E N T I A L SECTION 01 OF 04 COLOMBO 000540

SENSITIVE
SIPDIS

STATE FOR EEB/IFD/OMA BRIANA SAUNDERS AND SCA/INSB
TREASURY FOR SUSAN CHUN

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TAGS: [ECON](#) [EFIN](#) [PGOV](#) [CE](#)

SUBJECT: SRI LANKA: CB GOVERNOR RESPONDS TO U.S. IMF
CONCERNS

REF: A. COLOMBO 523
[1](#)B. COLOMBO 508
[1](#)C. OWEN-MOORE EMAIL 05/06/09
[1](#)D. COLOMBO 488
[1](#)E. SECSTATE 41959
[1](#)F. COLOMBO 449
[1](#)G. COLOMBO 431
[1](#)H. COLOMBO 385
[1](#)I. COLMOBO 285
[1](#)J. COLOMBO 244

Classified By: Ambassador Robert O. Blake, Reasons 1.4 (b)(d)

[1](#)1. (SBU) Summary: Central Bank Governor Nivard Cabraal, in a written response to DCM, classified U.S. attempts to "block" the GSL's IMF Stand-by Arrangement (SBA) as "misplaced" and "puzzling," noting that such an action could set a precedent for future IMF loan requests. Cabraal highlighted the GSL's excellent debt servicing record, its compliance with all IMF requests, and the country's ability to continue with its economic, social, and financial programs despite the conflict. He also lamented that the misinformation campaign against the GSL is painting an unfair picture of a government that deeply cares about the well-being of all of its people. Cabraal stated on May 18 that, despite efforts to look elsewhere for funds, the GSL remains keen to obtain an IMF SBA as it will lead to a positive impact on the economy and encourage post-conflict investment. End Summary.

[1](#)2. (SBU) In a written response (see para 6) to post's delivery of ref c points, on May 15 Central Bank Governor Nivard Cabraal called into question U.S. efforts to block or delay IMF facilities on political or non-economic factors, underscoring that the IMF's code of governance does not provide for the Executive Board to consider extraneous issues in its decision making. He warned that such actions may set a precedent for future IMF facilities. Cabraal highlighted that both the GSL's excellent debt service record and its ability to maintain economic, social and financial programs "in a satisfactory manner" throughout the conflict should lead the U.S. and others to the "logical conclusion" that ground conditions will ease following the end of the conflict, spurring Sri Lanka's economic and social development and the country's financial capabilities.

[1](#)3. (SBU) Cabraal also noted the GSL's strong commitment to develop the north quickly in order to improve the living conditions of its citizens, rather than to "impress" the international community. He wrote with dismay about the negative propaganda that have led others to believe that the

GSL's humanitarian practices have deteriorated.

¶4. (SBU) Perhaps in an effort to address U.S. concerns, Cabraal noted that as a result of the forthcoming defeat of terrorism, there is "now the real possibility of developing a time table and a definite set of strategies for the revival and reconstruction effort."

¶5. (C) Speaking with DCM and Econ Chief on May 18, Cabraal noted that the government was successful at increasing reserves in April, and will do so again in May. While positive that the government is slowly edging further away from a balance of payments crisis, he outlined that the government is still very keen to obtain an IMF SBA because of the positive effect it will have on the economy. However, in the meanwhile, he confirmed that the government is in talks with several other countries (Libya (USD 500mn), India (USD 600mn), China (amount TBD)) for loans. To date none of these loans have been finalized. Some may not be; Tourism Minister Milinda Moragoda told DCM on May 15 that the much-discussed Libya loan is in doubt.

¶6. (SBU) Substantive Language of the Letter:

Begin Quoted text:

Issues raised as per your note:

With regard to your request for an IMF stand-by arrangement, we are concerned about your ability and commitment to carry out an effective program in the current conflict

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circumstances.

Separately, your conduct in the final stages of this ear, and the way humanitarian issues are handled, will greatly influence your ability to reconcile and reconstruct your country after the conflict, and will also greatly influence the willingness of the international community to support you in your reconstruction efforts.

Until the humanitarian situation in the north is clarified, it will be difficult to assess the actual costs of meeting the immediate and longer term needs of the people, reconstruction, and further security expenditures. We urge you to improve your humanitarian practices with an eye towards gaining wide donor support for your near-term reconstruction needs.

The following are our broad reactions in relations to your concerns which views we shared with you at our meeting as well:

The conflict situation in Sri Lanka is not a current phenomenon or development. This conflict has been on-going in our country for over 25 years. During such period, while facing one of the most brutal terrorist groups in the world, our country has been able to continue with its economic, social and financial programs in a satisfactory manner. At the same time, it has also been able to maintain an impeccable debt servicing record without a single default. Further, during this period of prolonged conflict, the IMF has disbursed loans to Sri Lanka on eighteen occasions under nine facilities. In each such program, Sri Lanka has honoured its commitments and ensured that repayment is done without a single delay or default.

It is now common knowledge that Sri Lanka's terrorist conflict is reaching its final stages. Therefore, it would be logical to expect that the ground conditions would greatly ease after the conflict, so as to spur the country's economic and social development. In that scenario, it is likely that the financial capability of the country also correspondingly improve further. Thus, we would be able to fulfill the conditions of the proposed IMF program with even greater

confidence. As far as Sri Lanka's commitment towards debt servicing is concerned, the country has shown its deep commitment in no uncertain terms with an impeccable record of debt servicing. In fact, even on the day that the LTTE suicide bomb truck exploded its deadly cargo at the Central Bank headquarters in a fashion similar to the 9/11 Al-Qaeda attack at the World Trade Center in New York, the Central Bank staff, many of whom were gravely wounded, were at the disaster management site in a matter of hours after the blast, making the repayments that were due on that fateful day!

It must also be noted that the currently proposed facility of USD 1.9 billion is designed to be disbursed in several tranches over a 24 month period. Such periodic disbursements would be based on the effective fulfillment of the several program targets. If, therefore, the Sri Lankan authorities fail to implement any components of the agreed program, the next tranche could be held back by the IMF. Further, with regard to the disbursement of the first tranche, the Government and the Central Bank have already implemented all prior actions as agreed with IMF. Therefore, any concerns regarding the ability or the commitment on the part of the Sri Lankan authorities to adhere to an effective program, would be essentially misplaced.

For purposes of record, may we also state that the Sri Lankan authorities have already finalized each component of the Letter of Intent with the IMF staff and reached complete agreement on all key macro-economic targets and policies to be implemented under the program. Unfortunately however, we have been thereafter informally informed that the current delay in submitting the proposal to the Executive Board at the IMF is only due to the fact the US has indicated to the IMF Management that they want Sri Lanka's request for the stand-by facility delayed, which is obviously for reasons extraneous to economic factors.

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The second observation set out in your note is also puzzling to us. It is well known that the IMF's code of governance does not provide for the Executive Board to consider extraneous issues other than economic issues in relation to its decision making. In fact, were informed by reliable IMF sources that, in its long history, the IMF has never experienced any instances where member countries and/or Executive Board members have sought to "block" or delay facilities that have been finalized at the staff level, on political or non-economic issues. Your observation unfortunately encompasses a new dimension whereby extraneous matters which clearly stretch beyond the current mandate of the IMF are being brought into the IMF's decision-making process.

In recent past, the IMF has made many public pronouncements that the Fund is keen and willing to help member countries that have been adversely affected by the global financial crises. Further, in response to the current situation, several wealthy member countries have already pledged to augment the resources of the IMF by offering enhanced financing to meet funding for needy countries. In that light, it is naturally disappointing that the Sri Lankan stand-by arrangement is being delayed in a manner that is clearly contrary to the IMF objectives, governance structures, values, rules and conventions. Needless to say, such a "block" may also give rise to an unfortunate precedence which may be cited by others too, when IMF facilities are to be submitted for approval in the future.

In your note, we also observed that you have raised certain doubts regarding the commitment and ability of the Sri Lankan government to provide relief to internally displaced people and reconstruct the affected areas. In that regard, it should perhaps be noted that the Government has already demonstrated its ability and commitment by virtue of its

handling of the Eastern Province in the post-conflict period, in a very successful manner. In the East, not only has a substantial amount of investment already been made, but democratically elected local and provincial councils too have been established and are functioning in accordance with the law. Further, you may also particularly note that His Excellency President Mahinda Rajapaksa has recently appointed a high-level 19 member Task Force to deal with Resettlement, Development and Security in the North. All these actions, (not mere words), clearly confirm the Government's ability and commitment.

It has also been acknowledged by many, including those of the international community, that conditions in the Eastern Province have already returned to near normalcy in a very short period after a prolonged period of conflict. In fact, such an outcome has been achieved much earlier than the world community would have ever imagined. Elections have been held; economic activities have been revitalized and expanded; harmony within different ethnic groups has been established; infrastructure has been developed at a rapid pace; and most importantly, people of all races continue with their normal lives without fear or violence. Therefore, any misgivings and concerns about the Sri Lankan Government's ability to reconstruct the North in a very quick time would be clearly misplaced, in the light of the Government's exemplary track record.

In our own way, we at the Central Bank have been preparing ourselves to expand the banking system in the newly liberated areas by quickly facilitating the opening of many banking outlets by commercial banks. By doing so, we believe we would be in a position to implement new livelihood development programs impacting the people in the North. Needless to say, our focus and commitment to reconstruct these newly liberated areas, stems from our own intense desire to develop these areas expeditiously and thereby improve the living conditions of our people, and not so much to "impress" the international community. At the same time, as already indicated by His Excellency President Rajapaksa, we would certainly welcome the efforts of all nations towards this reconstruction effort and, in that context, we hope that the United States too would contribute actively to this endeavor, as indeed it has done in the past.

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It is now a well known fact that most of the criticisms and accusations leveled against the Sri Lankan Government have been cleverly organized and disseminated by pro-terrorist mis-information groups. In fact, the international media has been regularly embarrassed by the subsequent revelations made by the Sri Lankan authorities which have given lie to the many outrageous claims made by the mis-information groups. Nevertheless, those groups have been able to mislead many foreign governments, NGOs, etc, by their sustained campaigns. In particular, during the recent past, these false propaganda with even greater vigour in the face of massive defeats suffered by the terrorists at the ground level, and the reason for the build up of the perception that Sri Lanka's humanitarian practices have deteriorated, is essentially as a result of such major mis-information campaigns, and not because of the actions of the Government.

For the record, may we state that the Sri Lankan Government has always been deeply conscious of the well-being of all its people, while embarking on a tough battle to rid the country of the scourge of terrorism so as to liberate the people from the clutches of the LTTE. We must also understand that the war on terror is not an easy one. Terrorists resort to various ruses and practices to discredit those who oppose and fight terrorism. Terrorists have no sympathy for civilians and often subject them to violence in order to achieve their own objectives. The US has also experienced this situation and would therefore understand the challenge of dealing with terrorists who use innocent people as human shields. Today,

Sri Lanka is engaged in the largest ever hostage rescue operation in the history of the world, where thousands of our own citizens held hostage by the world's most ruthless terrorist group, are being systematically rescued. So far, the Sri Lankan forces have been able to rescue over 170,000 such hostages and more are being rescued daily. Further, as you may be aware, the LTTE terrorists are now confined to a small tract of land where our forces are bravely attempting to rescue the remaining trapped civilians held hostage. Even in these very trying and dangerous conditions, the Government has taken humanitarian approach where every precaution is being taken to ensure the safety of the civilian population. As a result of such actions, the capacity of the terrorist group is weakening rapidly and it is almost certain that, very soon, the entire country would be freed from the clutches of terrorism.

We also believe that the impending defeat of terrorism, there is now greater clarity in the humanitarian situation in the North. As a result, there is now the real possibility of developing a "time table" and a definite set of strategies for the revival and reconstruction effort. In fact, the present ground situation offers greater clarity than on 2nd March 2009, when Sri Lanka's request was first made to the IMF for the stand-by arrangement. According, we believe this new situation should provide the US Government with greater confidence in providing support for the near-term reconstruction needs, than in the recent past.

Finally, may we state that we are deeply appreciative of the frankness and candour with which we were able to discuss this issue with you. It is perhaps a reflection of the fact Sri Lanka and the United States have been countries with a history of excellent relations. We also believe that the USA, as the leading super power of the world, both militarily and economically, would not, in any way, want a large segment of Sri Lankan people who are emerging out of untold suffering at the hands of a terrible terrorist group, to suffer further as a result of a financing delay by the IMF and its resultant consequences. Accordingly, we do hope that this unfortunate issue could be quickly put to rest, and for Sri Lanka to receive the support of the US Executive Director on the Board of the IMF to approve our IMF facility. In that respect, we earnestly look forward to your Government's positive response. End quoted text.

BLAKE